



MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Auditors' Reports as Required by Office of
Management and Budget (OMB) Circular A-133 and
Government Auditing Standards and Related Information

Year ended June 30, 2006

MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Auditors' Reports as Required by Office of
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Exhibit I

Auditors' Report on Compliance with Requirements Applicable to Each Major Program, Internal Control over Compliance and Schedule of Expenditures of Federal Awards in Accordance with OMB Circular A-133

The Board of Trustees
Massachusetts Water Pollution Abatement Trust:

Compliance

We have audited the compliance of the Massachusetts Water Pollution Abatement Trust (the Trust), a component unit of the Commonwealth of Massachusetts, with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2006. The Trust's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal programs are the responsibility of the Trust's management. Our responsibility is to express an opinion on the Trust's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Trust's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Trust's compliance with those requirements.

In our opinion, the Trust complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2006. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questioned costs as item 2006-1.

Internal Control over Compliance

The management of the Trust is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Trust's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.



Exhibit I

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of the Trust as of and for the year ended June 30, 2006, and have issued our report thereon dated October 17, 2006. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards (Exhibit III) is presented for purposes of additional analysis as required by OMB Circular A-133, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended for the information of the board of trustees, management of the Trust, and the U.S. Environmental Protection Agency and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

October 17, 2006

MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Schedule of Expenditures of Federal Awards

Year ended June 30, 2006

Federal grantor/program title	CFDA number	Expenditures
U.S. Environmental Protection Agency:		
Capitalization Grant for Massachusetts Water Pollution Abatement		
Revolving Fund under Title VI of the Clean Water Act:	66.458	
2004		702,196
2005		35,900,683
Total		36,602,879
Capitalization Grant for Massachusetts Water Pollution Abatement		
Revolving Fund under the Federal Safe Drinking Water Act,		
Section 1452:	66.468	
2002		278,887
2003		3,769,090
2004		6,141,440
2005		17,901,837
Total		28,091,254
Total expenditures of federal awards		\$ 64,694,133

See accompanying notes to schedule of expenditures of federal awards.

MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Notes to Schedule of Expenditures of Federal Awards

Year ended June 30, 2006

(1) Definition of the Reporting Entity

The Massachusetts Water Pollution Abatement Trust (the Trust) is an authority established by the laws and is a component unit of the Commonwealth of Massachusetts (the Commonwealth). The accompanying schedule of expenditures of federal awards presents the activity of all expenditures of federal awards of the Trust. All expenditures of federal awards received directly from federal agencies are included on the schedule.

(2) Summary of Significant Accounting Policies

The Trust's accounting policies conform with generally accepted accounting principles applicable to governmental units as set forth by the Governmental Accounting Standards Board.

Basis of Presentation

The accompanying schedule of expenditures of federal awards is presented using the accrual basis of accounting.



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Exhibit III

**Report on Internal Control over Financial Reporting and on Compliance and
Other Matters Based on an Audit of Financial Statements Performed
in Accordance with *Government Auditing Standards***

The Board of Trustees
Massachusetts Water Pollution Abatement Trust:

We have audited the financial statements of the Massachusetts Water Pollution Abatement Trust (the Trust), a component unit of the Commonwealth of Massachusetts, as of and for the year ended June 30, 2006, and have issued our report thereon dated October 17, 2006. We conducted our audit in accordance with U.S. generally accepted auditing standards and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the Trust's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting or its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Trust's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements or other matters, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We also noted certain additional matters that we reported to management of the Trust in a separate letter dated October 17, 2006.



Exhibit III

This report is intended solely for the information and use of the board of trustees, the management of the Trust, and the U.S. Environmental Protection Agency and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

October 17, 2006

MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

(1) Summary of Auditors' Results

(a)	Type of report issued on the financial statements:	Unqualified
(b)	Noncompliance which is material to the financial statements:	None reported
(c)	Reportable conditions and material weaknesses in internal control disclosed by the audit of the financial statements:	None reported
(d)	Reportable conditions and material weaknesses in internal control over major programs:	None reported
(e)	Type of report issued on compliance for major programs:	Unqualified
(f)	Audit findings required to be reported under Sec. 510(a) of OMB Circular A-133:	Yes
(g)	Major Program:	

<u>Funding source</u>	<u>Program</u>	<u>CFDA number</u>
U.S. Environmental Protection Agency	Capitalization Grant for the Massachusetts Water Pollution Abatement Revolving Fund under the Title VI of the Clean Water Act	66.458

(j)	Dollar Threshold Used to Distinguish Type A and Type B Programs:	\$1,919,758
(k)	Qualification of Auditee as a Low-Risk Auditee:	No

(2) Findings Relating to Financial Statements Reported in Accordance with *Government Auditing Standards*

None

(3) Findings and Questioned Costs Relating to Federal Awards

Finding number:	2006-1
Federal Agency and Pass through Entity:	Environmental Protection Agency
CFDA number:	66.458
Program:	Capitalization Grants for Clean Water State Revolving Funds
Finding:	Subrecipient Monitoring

MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Description:

As set forth in the 31 USC 7502(f)(2)(B)(Single Audit Act Amendments of 1996(Pub. L. 104-156)), OMB Circular A-133 (§__.225 and §__.400(d)), A-102 Common Rule (§__.37 and §__.40(a)), Environmental Protection Agency program regulations, and the terms and conditions of the award, a pass-through entity is responsible for:

- *Award Identification* – At the time of the award, identifying to the subrecipient the Federal award information (e.g., CFDA title and number, award name, name of Federal agency) and applicable compliance requirements.
- *During-the-Award Monitoring* – Monitoring the subrecipient’s use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- *Subrecipient Audits* – (1) Ensuring that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003 as provided in OMB Circular A-133, as revised) or more in Federal awards during the subrecipient’s fiscal year have met the audit requirements of OMB Circular A-133 (the revised circular is available on the Internet at <http://www.whitehouse.gov/omg/circulars/a133/a133.html>) and that the required audits are completed within 9 months of the end of the subrecipient’s audit period, (2) issuing a management decision on audit findings within 6 months after receipt of the subrecipient’s audit report, and (3) ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.
- *Pass-Through Entity Impact* – Evaluating the impact of subrecipient activities on the pass-through entity’s ability to comply with applicable Federal regulations.

During our review of the subrecipient monitoring process at the Trust, we noted that “during the award monitoring” or programmatic monitoring is performed of certain of the Trust’s loan recipients. This process is carried out by the Massachusetts Department of Environmental Protection, Division of Municipal Services. However, we noted that these and other prior year loan recipients may not have been notified by the Trust, either through the loan agreements or through a separate correspondence, that the loan proceeds were to be considered Federal funding for OMB Circular A-133 and as such, the Trust did not request or obtain Single Audits from the appropriate loan recipients. As such the Trust did not appear to have controls in place to comply with and did not comply with the “Award Identification” and “Subrecipient Audits” requirements noted above.

Questioned costs: Not able to determine

MASSACHUSETTS WATER POLLUTION ABATEMENT TRUST

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Recommendation:

We recommend that the Trust management confer with the Regional EPA officials regarding the interpretation of the subrecipient monitoring requirements related to its Federally Funded Capitalization Grant Programs to ensure that loan recipients under these programs should be considered subrecipients and not treated as vendors. Once agreed to, the Trust should memorialize the requirement to ensure that the agreement is properly executed in the future.

Management's Response

The Water Pollution Abatement Trust has relied upon an interpretation of OMB Circular A-133 that would classify recipients of leveraged loan funds as "vendors," an interpretation that until now had not been questioned under audit or program review. It is our view that under this interpretation, the Trust is in full compliance with EPA and OMB requirements.

However, based upon this finding, the Trust will follow the recommendation that we confer with EPA Region 1 to determine the proper interpretation of OMB Circular A-133 as it pertains to the specific circumstances of the State Revolving Fund program. We will memorialize our understanding of this matter, and will ensure proper execution prospectively. We expected to resolve this finding by June 30, 2007.

Management's Contact

Scott Jordan, Executive Director
617-367-9333 x579